

Austin - Direct

101

1 A. Yeah, one more time, please.

2 Q. One more time. Why was emerging as quickly as possible a
3 goal of the company -- emerging from Chapter 11?

4 A. Well first of all, as I said, our relationship with the
5 regulators was not at its zenith at the time and we felt that
6 in order to preserve the -- and enhance the estate, enhance the
7 assets, minimize the costs that are involved in a Chapter 11
8 proceeding. And to do this -- to do this on a quick basis was
9 in the best interest of the estate.

10 Q. So to kind of recap, Mr. Austin, you filed Chapter 11 now,
11 you had the efforts pre-bankruptcy to try and restructure out
12 of proceedings, you now filed Chapter and you developed a list
13 of goals of trying to stabilize the business, correct?

14 A. That's correct.

15 Q. Rebuilding liquidity?

16 A. That's correct.

17 Q. Sell off the non-core business?

18 A. That's correct.

19 Q. And focus on the core utility assets?

20 A. That's right.

21 Q. And then to focus on converting the unsecured debt to
22 equity?

23 A. That was the plan.

24 Q. And rebuild the relationship with regulators and to emerge
25 as quickly as possible?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

102

1 A. That's right.

2 Q. Now, let's focus on the goal -- 'cause I think you talked
3 about rebuilding liquidity. You did that with the DIP loan,
4 correct?

5 A. We did, that was our backstop.

6 Q. And then -- just on that --

7 A. I would add that we used that DIP loan to the tune of about
8 13 or \$14 million only for letters of credit to backstop some
9 of our vendors, but we never actually borrowed under that DIP
10 facility. Basically because we focused on the cash generation
11 and liquidity from the operation so we had a very successful
12 processing.

13 Q. So you definitely achieved that goal?

14 A. We did.

15 Q. Let's focus on the business and the stabilization. Did
16 that focus on both the operation as well as the financial?

17 A. Yes, it did.

18 Q. All right, and when you were looking at that, what was the
19 focus of trying to develop both a sound business plan and a
20 financial model?

21 A. Well, we had had a financial plan in the summer of 2003.
22 What was clear is that it was not a tightly developed plan, it
23 was not a bottoms-up plan. And we had to develop a plan that
24 the management team, including all of the operational people
25 and all of the divisional people, bought into. So we spent the

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

103

1 -- really the late summer and the fall of 2003 developing a
2 financial plan that everyone could buy in, whether it be the --
3 at the divisional level all the way up to the Chief Operating
4 Officer and the CEO. So we developed a rigorous, thoughtful
5 financial plan, which was the first one that was developed at
6 the company.

7 Q. And that was what I was gonna ask you was how did you
8 believe, based on your experience at the company, how to
9 develop that -- we'll call it the -- let's refer to it as the
10 5-year business plan -- how did it compare to what had --
11 previous plans that had been developed by the company?

12 A. Well again, you had to recognize that this company had only
13 owned -- when the first plan was developed -- the first plan
14 that I saw, which was in the early part of 2003, that was a
15 plan that was developed and the company had only owned Montana
16 for a little less than a year at that point. So a lot of those
17 plans were top-down, financial projections, and did not have
18 the buy-in of all the people below the financial planners, if
19 you will. It didn't have all the operational buy-in. So, the
20 plan that we were operating to in 2003 was one that we were
21 clearly not achieving those plans. Some of it was due to the
22 liquidity and the stress that was put on the company. But some
23 if it the plan just was an overly aggressive plan. So, as we
24 headed into the bankruptcy process, we had to develop a plan
25 that was more of a bottoms-up plan; was rigorously bought in

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

104

1 by all of the constituencies.

2 Q. All right, what was your perspective, if any, of the
3 reliability of Northwestern's forecast and projections in the
4 September or October, early November timeframe?

5 A. Well, they were getting better with each passing cut of the
6 plan. I mean, basically we developed a plan and went through a
7 number of modifications. In fact, a number of the cost
8 elements that were later introduced into the plan were
9 recognized, if you will, during that time period. As a for
10 instance, we didn't have in the original plan that was -- what
11 I'll call it 2003 plan -- we didn't have an original cost in
12 there for the pension expense. And as we studied the pension
13 expense and the funding that the company had at that time, it
14 was clear that we had that we had to put in a substantial
15 change into the pension expense line, which went into the G&A
16 line of the forecast.

17 Q. Do you recall how much was added for pension obligations or
18 expense throughout -- say for 2005?

19 A. I think we added in the final analysis it was a \$19.6
20 million add to the pension plan at that time.

21 Q. And just to isolate that, did that have any --

22 A. I'm sorry, what it was -- it was 10.6 for the 2003, but on
23 the go forward basis, it was closer 19 a year.

24 Q. And just to isolate that one item, what impact, if any, did
25 that have on the company's EBITDA?

Writer's Cramp, Inc.

Certified Court Transcribers

732-829-0191

Austin - Direct

105

1 A. Well, it would be a direct cost to the EBITDA, so it'd take
2 the EBITDA down by that 19.6 or in -- for 2003, took it down by
3 the 10.6. For the 2005 and beyond, it took it down by almost
4 19½ -- \$19.6 million.

5 Q. And that additional pension obligation, for example, was
6 not embedded in the initial runs and numbers, say, in October,
7 to your knowledge?

8 A. I don't know if it was in -- it certainly wasn't in the
9 middle of the summer, I don't know if was -- we captured it in
10 October or not.

11 Q. From your perspective, when was there available the first
12 good numbers of the 5-year business plan?

13 A. The first number -- and we went through, as I said, a more
14 rigorous and discipline process in then we presented the
15 results of that in early December to the Board. And the Board
16 of Directors approved that plan. We later presented that plan
17 to the Creditors' Committee. But those were the first, what I
18 would call, rigorously done -- professionally done, financial
19 plans for the core business, the core business that was left
20 behind, that the company did. Period.

21 Q. And, when you say the first time that business plan was
22 presented to the Creditors' Committee was in mid-December?

23 A. Mid-December, that's correct.

24 Q. Now, is that 5-year business plan -- is that the business
25 plan and projections that serve to support the Northwestern's

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

106

1 proposed reorganization plan?

2 A. It is. I think there's been a few minor tweaks to it, but
3 the genesis of the plan is the plan that we developed for that
4 December of 2003.

5 Q. And from your perspective, any modifications from December
6 to today, for example, have been just small updates, technical
7 amendments (inaudible)?

8 A. Yeah, updates -- there've been updates for cash. We've
9 done a little bit better on the cash generation than what was
10 in the plan. But the fact of the matter is, as we look at that
11 plan for 2004, we're behind that plan. So while there's a
12 great deal of effort to say that that plan is a low-ball plan,
13 the fact of the matter is, we're behind that plan from an
14 EBITDA standpoint. Now, we're ahead of the plan from a cash
15 standpoint, but from an EBITDA standpoint, we're behind that
16 plan.

17 Q. Now, from your perspective, how would you compare, say if
18 it's better or worse or no real change, how would you compare
19 the 5-year business plan supporting the Debtor's Reorganization
20 Plan to the projections that were that were developed in the
21 October/November 2003 timeframe?

22 A. Well you know, the discipline in the plan, the ability for
23 us to measure and manage that on a monthly basis now is far
24 superior to anything that we had in the summer and fall of
25 2003. And part of that is we brought in a new CFO, a CFO who

Witter's Cramp, Inc.

Certified Court Transcribers

732 329-0191

Austin - Direct

107

1 has helped with the discipline on the plan and the reporting
2 process. And we're -- you know, the company now can operate in
3 a much more stable business environment.

4 Q. Now, you developed the projections in this 5-year business
5 plan, you presented to the Creditors' Committee in a mid-
6 December timeframe 2003. Prior to that, I think you testified
7 there was no preconception about how any new equity and
8 restructure in Northwestern would be divided between the senior
9 unsecured notes and subordinated, correct?

10 A. That's right. Our objective was to clearly manage or -- to
11 optimize the value of the estate and not figure out who was
12 gonna own what.

13 Q. But was your perspective that there was no value to equity?

14 A. That's correct. When we added up the value that we got,
15 approximately it's about -- actually approximately it's the
16 value that we have today, it was about a billion six, in total
17 value of the company -- of the entity.

18 Q. So that December evaluation indicated a value of
19 approximately \$1.6 billion?

20 A. That's correct.

21 Q. And that has not really shifted very much since then,
22 correct?

23 A. Some of the elements have shifted, we -- in early December,
24 we thought, in fact, that we had more value coming from the
25 non-core assets and, in fact, we've had less value. We thought

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

108

1 we were gonna have less cash flow coming from the main
2 operations, in fact we had a little more value.

3 MR. MORRIS: Your Honor, I'm gonna object to that last
4 question -- the last question before that was --

5 THE COURT: You need to state your name counsel.

6 MR. MORRIS: I apologize. My name is John Morris, I'm
7 from Kronish Lieb, I'm for the equity holders Kellogg Capital
8 and RCG Carpathia. I've been very lenient, especially in the
9 background. We're getting into substance and I would just
10 request that Mr. Austin not lead the witness on these important
11 figures.

12 MR. AUSTIN: That's fine, Your Honor.

13 THE COURT: All right.

14 BY MR. AUSTIN:

15 Q. Mr. Austin, what is your perspective on whether management
16 has included or not included all material factors in it's 5-
17 year business plan of projections?

18 A. We've tried very diligently, as had the rest of the
19 management team, to identify and consider all major factors in
20 our business plan.

21 Q. And you're familiar with that business plan, correct?

22 A. I am.

23 Q. One of the elements of that business plan is the -- I
24 believe, that there's a need for approximately \$35 million in
25 cash at all times to be retained by reorganized Northwestern?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

109

1 A. What we've projected in -- as you identify what your
2 liquidity needs are, both from a rating agency and from a
3 vendor standpoint, we chose that \$35 million number. And I
4 think that it shows as of September of 2004 that \$35 million
5 number. In fact, what happens during the winter season is that
6 some of that liquidity will be used up because as you go into
7 the heating season, we have to buy a lot more gas, we have to
8 buy a lot more electricity. And our need for financing, if you
9 will, working capital financing, increases during the -- I
10 think peaks sometime in January. So the \$35 million may be the
11 number at September 30th. That would decrease going into the
12 winter season.

13 Q. If the cash was used, is that correct?

14 A. If the cash was used or the debt -- we also plan of having
15 a hundred million dollar exit revolving credit facility.

16 Q. Well, if the company is able to attain a working capital
17 credit line, can you explain why there's a need to also retain
18 \$35 million in cash from the voucher?

19 A. Well, you really want a combination of the two. Do you
20 need \$35 million everyday? Absolutely not. That's a good
21 place holder so that you operate. As I said, in some cases
22 you'll have \$35 million, as you go into the winter season, it
23 might drop down to 5 or \$10 million. As long as you have that
24 backstop or that working -- the revolver, you're fine. But the
25 rating agencies and your vendors are looking for some liquidity

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

110

1 measure in the form of cash on the balance sheet, I believe.

2 Q. Let's focus on two other general areas of inquiry before we
3 finally conclude your examination. First is an area referred
4 to, I think you've (indiscern.) QF.

5 A. Right.

6 Q. Can you explain what a QF?

7 A. A QF stands for Qualifying Facilities. It's a third party
8 energy producer and generally an alternate -- alternative
9 energy wind, Wing Cogen, hydro, that we enter into contracts
10 with these third party power generated. It's under FERC
11 regulations. It's under -- I should say federal regulation,
12 but we enter into these facilities as part of our default power
13 supply from Montana. I think there's approximately 19 of them
14 that we have.

15 Q. Is there any liability recorded on the company's balance
16 sheet related to these QFs?

17 A. We record the liability and the reason for that liability
18 is that the amount of contractual obligations we have for these
19 qualifying facilities is greater than the amount that we can
20 recapture as we pass through to our customers. And the amount
21 that we have listed as a balance sheet item is 140 --
22 approximately \$140 million.

23 Q. And that's calculated how?

24 A. It's a fairly -- I was about to say simple calculation.

25 It's calculation that looks at the amount that we pay out over

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

111

1 the next, in some cases, 26, 27 years, and the amount that we
2 are allowed to pass through in the form of charges to our
3 customers. The difference is a cash flow stream, again, over
4 this about 26, 28 year period. We take that negative cash flow
5 stream and discount it back to present value and use that
6 discounted value and that comes up with \$141 million.

7 Q. Can you describe what actions, if any, were taken to try
8 and reduce that liability?

9 A. We did analyze the QFs. We looked at as to whether or not
10 we could, in fact, reject them as executory contracts. We
11 tried to run a calculation as to if they were rejected, what
12 would be the claim. If they were rejected, what would be the
13 resultant response from Montana and specifically consumer power
14 -- I'm sorry, the Consumer Counsel in Montana, because to that
15 extent that we achieved some benefit by the rejection or the
16 renegotiation, if you will, of those qualifying facilities,
17 some of those benefits might be claimed by the Consumer Counsel
18 and from the Montana PFC at that point. So, we looked at them,
19 we determined that it was really not in the best interest of
20 the estate to reject them because the claims would be greater
21 than the benefit that we would accrue to the company.

22 Q. Just on a rough basis, could you -- do you recall what may
23 have been the general claim that may have resulted if the
24 company could have rejected the QF contracts?

25 A. Well, the total amount of contractual obligation that we

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

112

1 had in the QFs was almost \$2 billion. And in taking -- you
2 could have had claims at or -- and that was our calculation,
3 depending on what the QF parties -- the third parties came up
4 with. They may have come up with claims higher than that in
5 fact.

6 Q. Is that gross or is that a present value note?

7 A. That's a gross number.

8 Q. Now, one more question of QFs.

9 A. Actually, to correct the record, I think it's actually
10 higher than that. And for the life of me, I can't remember the
11 exact number. I think the gross number is actually higher than
12 1.9 million, but --

13 Q. These QF contracts, as you explained it, are actual
14 contractual agreements for the company to purchase power, is
15 that correct?

16 A. That's correct.

17 Q. Now, based on your experience, Mr. Austin, if a third party
18 came in to acquire Northwestern, what impact, if any, would
19 this \$140 million liability have on the purchase price?

20 A. Well, if I were looking -- and I did some of this analysis
21 back when I was in the leveraged buyout business -- but if I
22 looked at an obligation like this, it's a true cash obligation
23 and I would subtract it from the valuation that I would be
24 willing to pay for any company.

25 Q. Now another asset which the company is identifying in its

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

113

1 Reorganization Plan is net operating losses. Are you familiar
2 with those on a general basis?

3 A. On a general basis, absolutely.

4 Q. All right. Do you have an understanding of whether there's
5 any change in the value of the NOL with the company that
6 utilized from say, early December to sometime later?

7 A. When we originally looked at the NOL situation, which would
8 have been in the summer of 2003, at that time our calculation
9 came up with -- and our calculation was done basically with
10 Deloitte & Touche and the help of their tax experts. We
11 calculated some \$735 million of NOL's. That subsequently has
12 been reduced, primarily because of a re-look at the NOL
13 calculation by Deloitte & Touche later in that year. Actually
14 it would have been early in 2004 when the recalculation was
15 done.

16 Q. So that's just for a final re-analysis?

17 A. Yeah, these are -- I wouldn't say they're arcane, but
18 they're intricate calculations, and depending on what --
19 depending upon the operating history of the company and how
20 Deloitte & Touche looks at those numbers, they can change from
21 time to time.

22 Q. Mr. Austin, you identified, I think, a number of goals that
23 this company had, Northwestern had at the beginning of this
24 Chapter 11 case. Sitting here today, what is your perspective
25 that if this Debtor's Plan is confirmed of what's been

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

114

1 accomplished by this Debtor? Have those goals been
2 accomplished from this case?

3 A. I think a great deal has been accomplished. You know, the
4 company is now operating in a very stable situation. It's
5 improved its relationships with the regulators, it's built
6 liquidity, it's sold primarily the non-core assets, although we
7 still have a little bit to go. It should come out as a near
8 investment grade -- and I say near, because I don't think we'll
9 achieve the investment grade status on the first -- upon
10 emergence. But I think a lot has been accomplished and I think
11 the company is now a stable company that should emerge as a
12 quality operating company.

13 Q. Based on your understanding of the company, your
14 familiarity with the company and this proposed Reorganization
15 Plan, do you have a perspective on whether the recoveries under
16 the Reorganization Plan would be better than if Northwestern
17 were to be liquidated?

18 A. Well, we have, during this timeframe, entertained a number
19 of offers from strategic buyers that have offered to buy the
20 company -- or, I shouldn't say offered, they've shown some
21 indications of interest. We were never able to get a firm
22 offer, I would add, but those indications of interest were all
23 at or below the value that we think was gonna come out of the
24 emerged company here. So, I think as an emerged company, this
25 the best thing for the Debtor to do.

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Direct

115

1 Q. Mr. Austin, if this Plan is confirmed, do you have a
2 perspective as to whether Northwestern will be able meet the
3 obligations it providing for under the Reorganization Plan and
4 not have to go through further restructuring?

5 A. I believe it's a stable Plan, the company -- it's a stable
6 operation and can meet its debt obligations and note
7 obligations as they come due.

8 Q. Do you have a perspective today whether there is any
9 distributal value to Northwestern's equity holders?

10 A. I do not believe there is any distributal value, based on
11 the waterfall analysis and based on the value that we've worked
12 at in conjunction with our advisors.

13 Q. If there's any significant additional delay in Northwestern
14 obtaining confirmation of this Plan and exiting Chapter 11, do
15 you have a perspective whether there would be any impact on the
16 value that is proposed to be distributed to Northwestern
17 Creditors?

18 A. Well, one of issues and one of the reasons for speed in
19 this case is that the company -- well, it's got a stable EBITDA
20 and a stable financial projection. It does trade as an
21 interest sensitive stock, or it should, I believe, should trade
22 as an interest sensitive stock. And if you look at interest
23 rates today versus what they'll be in 3 months -- and while I'm
24 not a soothsayer on that -- I think the pressure for interest
25 rate increases is higher than interest rate decreases. And the

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

116

1 sooner we get out, do our exit financing, I think the more
2 value the company will have. That's just from the investment
3 banking side. From the standpoint of staying in bankruptcy and
4 incurring the kinds of costs that we're incurring today, I
5 think is a detriment to the estate. So, the sooner we get out,
6 I think, the better it is.

7 Q. I assume present company excepting that?

8 A. No, I wouldn't even except that.

9 MR. AUSTIN: Your Honor, that's all the questions I
10 have for Mr. Austin.

11 THE COURT: All right, is there anybody who has
12 questions of Mr. Austin who is a proponent of the Plan?

13 ALL: (No verbal response).

14 THE COURT: If not, is there any cross examination
15 from any objector?

16 MR. MORRIS: Yes, Your Honor. Just a few questions.
17 Again, John Morris for the equity holders.

18 CROSS EXAMINATION

19 BY MR. MORRIS:

20 Q. Good afternoon, Mr. Austin.

21 A. Good afternoon, John.

22 Q. I think you said that at the time the company went into
23 Chapter 11 it did not have a good relationship with state
24 regulators, is that correct?

25 A. I would say that is correct.

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

117

1 Q. And in fact, it was a poor relationship, is that correct?

2 A. I would characterize it as poor.

3 Q. And that was in part because of the decision by
4 Northwestern to extend the payment of taxes back in June as you
5 described, is that right?

6 A. Well, I think that's a little bit -- I think it ran a lot
7 deeper than just a non-payment of real estate taxes.

8 Q. I'm just asking, is that one particular reason?

9 A. I think that's one.

10 Q. And another particular reason was a consequence of
11 Northwestern's decision to attempt to diversify, is that right?

12 A. That's correct.

13 Q. And go into all of these other businesses outside of their
14 core energy business, is that right?

15 A. It's clear that the diversification strategy was poorly
16 contemplated and poorly executed.

17 Q. And it was poorly received by the regulators, isn't that
18 right?

19 A. And it was poorly received by the regulators.

20 Q. And it was poorly executed as well, isn't that right?

21 A. That is correct.

22 Q. These were losing propositions?

23 A. Yes, Sir.

24 Q. And the regulators didn't want the rate payers,
25 Northwestern's company -- customers to pay for the strategic

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

118

1 mistakes made by Northwestern, is that correct?

2 A. I think that is an accurate assessment of their position.

3 Q. And to address those concerns that we've just talked about,
4 Northwestern has, in fact, either sold or will shortly sell off
5 it's non-core businesses, is that right?

6 A. That's right. It will revert back to it's core utility
7 business, that's correct.

8 Q. And was there a settlement recently reached with the
9 Montana Public Service Commission?

10 A. There has been, yes.

11 Q. Can you describe that for the Court?

12 A. Well, I -- in general, it's a settlement as to how the
13 company will operate on a going-forward basis. It does
14 ascribe, or prescribe, us to stay as a core gas and electric
15 utility business. And it has certain restrictions and certain
16 reporting requirements and the like. But basically what it
17 says is we're gonna operate in the -- in a stable, straight-
18 forward manner in the utility business.

19 Q. And that's something that I take it was a positive
20 development vis-a-vis Northwestern's relationship with the
21 regulators?

22 A. I believe it has been, yes.

23 Q. Okay. If one of the goals with -- of Northwestern in
24 entering Chapter 11 was rebuilding its relationship with the
25 state regulators, and we've identified the settlement and the

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

1 sale of the non-core businesses, what other steps has
2 Northwestern taken during the pendency of the bankruptcy case
3 to improve its relationship with the state regulators?

4 A. Well, I think one thing is the frequency of contact and the
5 openness of the communication. And I think we've tried to do
6 that and I think -- and I hope it's been appreciated by the
7 regulators. I mean, we owe it to the regulators to be forth
8 right and up front an open in terms of our finances and our
9 communications. And I think we've gone a long way to doing
10 that. Whether or not they all believe that yet, I don't know.

11 Q. But it is your understanding heading into bankruptcy that
12 one of the concerns the regulators had about Northwestern was
13 its lack of openness, is that right?

14 A. That's my understanding.

15 Q. And to the best of your knowledge, Northwestern has done
16 all it could to address that particular concern, is that right?

17 A. We are trying, yes, Sir.

18 Q. Are there any other ways in which Northwestern has
19 attempted to improve its relationship with state regulators?

20 A. I can't think of any others.

21 Q. But it is your belief that today Northwestern has a much
22 better relationship with the regulators than it did prior to
23 the time it entered bankruptcy, correct?

24 A. I believe it to be so, yes.

25 Q. You talked a bit about the projections, do you recall that?

Austin - Cross

120

1 A. I do.

2 Q. And over time, beginning last summer through the end of the
3 year, the projections got better and better with each cut of
4 the plan, is that right?

5 A. I believe they got more disciplined and more accurate,
6 that's correct.

7 Q. And one of the things that was a result of that process was
8 the inclusion of these pension expenses that you talked about,
9 is that right?

10 A. That's correct.

11 Q. And the projections now include approximately \$20 million
12 per year in pension expense throughout the projection period,
13 is that right?

14 A. That's correct.

15 Q. And is that today the company's best estimate of what the
16 pension expense will be over that time?

17 A. To the best of my knowledge, that's the -- there'll be some
18 tweaks from time to time and we'll look at it every year, but
19 that's our best guess at this point.

20 Q. Okay. But it is the company's position that the
21 projections today fully reflect the pension expense that's
22 expected over time?

23 A. Yes.

24 Q. And in fact, in creating the projections Northwestern tried
25 diligently to consider all of the major factors in creating the

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

121

1 projections, is that right?

2 A. I believe we did.

3 Q. Just a couple of more questions, Mr. Austin, and thank you
4 for your patience. You talked for a few minutes about the net
5 operating losses, do you remember that?

6 A. Yes.

7 Q. And you said that in the summer of 2003, Deloitte's best
8 estimate at that time was that they were available \$735 million
9 of net operating losses, is that right?

10 A. Right, that's my recollection and that would have been as
11 of the date of emerge -- what we always do is we look at the
12 net operating losses as the date that we plan to emerge. So if
13 we look at it at 735, we looked at it such that it -- that's
14 what we would calculate it would be at the date of emergence.

15 Q. And when you talk about the date of emergence, you're
16 talking about the period of time immediately after the Plan is
17 confirmed and the company is no longer in bankruptcy, is that
18 right?

19 A. That's right, and we always estimated that at about
20 September 30th of this year.

21 Q. And so that would also be the time in which the conversion
22 of debt to equity has already been accomplished?

23 A. Right.

24 Q. What is your understanding of the current best estimate of
25 the value of the NOLs?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

122

1 A. It's somewhat less than that, I don't know the exact
2 number, but it's less than that.

3 Q. Is it fair to say it's north of 600 million?

4 A. I think it is north of \$600 million.

5 Q. No further questions, Your Honor.

6 THE COURT: Okay, anybody else have any questions?

7 MR. HOUSTON: Yes, Your Honor, this is Joseph Houston
8 here for Mr. Hylland.

9 THE COURT: All right, Mr. Houston.

10 MR. HOUSTON: Thank you, Your Honor.

11 CROSS EXAMINATION

12 BY MR. HOUSTON:

13 Q. Sir, I'm assuming that you are familiar with the name
14 Richard Hylland?

15 A. I am.

16 Q. And I'm assuming that you are familiar that he has filed an
17 objection -- a limited objection to the proposed Plan of
18 Reorganization, correct?

19 A. That's my understanding.

20 Q. And do you know what the nature of his objection is?

21 A. Frankly, I do not.

22 Q. Well, I'll tell you that one of them is that the way in
23 which to -- the proposed distribution (inaudible) relating to
24 the D&O Trust is set up is unfair and discriminatory. Are you
25 aware of that?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

123

1 A. As I said, I'm not aware of how (inaudible).

2 (Telephone connection interference)

3 Q. Can you hear me?

4 A. I said I'm not aware of how his objection was
5 characterized.

6 Q. Well, Mr. Hylland has objected on the basis, in part, that
7 the manner in which the D&O Trust is set up is FIFO. Are you
8 familiar with the term FIFO?

9 MR. AUSTIN: Your Honor, I'd like to raise an
10 objection that this cross examination is beyond the scope and
11 it also -- of the Direct examination, and also that he's really
12 arguing confirmation issues.

13 THE COURT: Well, it strikes me more as argument. The
14 witness has already indicated that he is not familiar with the
15 Hylland objection.

16 A. Right.

17 THE COURT: So I think there may be a lack of
18 foundation here. Where are you going with this, Counsel?

19 MR. HOUSTON: Well Your Honor, I want to see if this
20 witness understands what the term FIFO is and whether this
21 witness is -- adopts the {quote} "Debtor's response" to Mr.
22 Hylland's objection with respect to this trust. And I think
23 that -- and I also have a couple of factual questions that I
24 need to establish from him.

25 THE COURT: I think you ought to go to the factual

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Cross

124

1 issues because I think the others are argument, and those can
2 be raised, those are preserved. But the witness has already
3 testified that he doesn't -- he's not familiar with the Hylland
4 objection. So why don't you move onto the factual issues as to
5 which this witness may have some information.

6 MR. HOUSTON: Very good, Sir.

7 BY MR. HOUSTON:

8 Q. Sir, do you understand the term FIFO, F-as in Fred, I-F-as
9 in Fred, O?

10 THE COURT: No.

11 MR. AUSTIN: Objection, Your Honor.

12 THE COURT: Sustained. That's not what I want you to
13 talk about. I don't think that's within the scope of what this
14 witness has indicated he had foundation to talk about. So I
15 think you ought to -- if you have factual questions, please ask
16 them.

17 MR. HOUSTON: Very good.

18 BY MR. HOUSTON:

19 Q. Sir, is it your understanding of the operation of the D&O
20 Trust that if there are let's say, for example, 28 claimants to
21 the Trust, and that happens to be the number of class 12
22 ballots that were reflected in the voting. If there are 28
23 claimants to the Trust and let's say claimants numbers one
24 through 25 submit claims and exhaust the trust, that claims
25 numbers 26 through 28 get zero?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Redirect

125

1 MR. AUSTIN: Objection, again, Your Honor, same basis
2 as before. He's just going at it at a different angle.

3 A. I don't pretend to be qualified to talk about the
4 channeling trust and --

5 THE COURT: Sustained.

6 MR. HOUSTON: Very good, Sir. Nothing further.

7 THE COURT: All right, thank you. Anybody else have
8 anything --

9 MR. MORRIS: In fact, nothing at all, I guess,
10 actually.

11 (Laughter)

12 MR. HOUSTON: Very good, Sir. Nothing further.

13 THE COURT: All right, thank you. Anybody else --

14 MR. HOUSTON: In fact, nothing at all, I guess
15 actually.

16 (Laughter)

17 MR. AUSTIN: Your Honor, I have one comment to make
18 and I have then -- I'd like to ask one question on redirect.
19 And I will get my question out of the way and then I'll do my
20 comment.

21 REDIRECT EXAMINATION

22 BY MR. AUSTIN:

23 Q. Mr. Austin, as relates to the sale of the non-core
24 business, which you had previously testified to, do you have a
25 perspective as to whether the Debtor will actually have access

Writer's Cramp, Inc.

Certified Court Transcribers

132-329-0191

Austin - Redirect

126

1 to the cash from the disposition of those non-core assets such
2 as the Cornerstone note, Expanets and Blue Dot and MFN by, for
3 example, October 30th?

4 MR. RATNER: Objection, this is beyond the scope of my
5 cross.

6 MR. AUSTIN: You asked a question about timing on the
7 non-core assets.

8 MR. RATNER: I don't believe I did at all, Your Honor.
9 All I did was ask whether or not the sale of the non-core
10 assets satisfied one of the concerns of the regulators.

11 THE COURT: Overruled.

12 BY MR. AUSTIN:

13 Q. You can answer the question.

14 THE COURT: Can you answer the question?

15 A. I don't believe we'll have access -- we may have access to
16 some small amount from Blue Dot, but we will not have access, I
17 don't believe, from the sale of the other (inaudible).

18 MR. AUSTIN: Your Honor, that's all the questions I
19 have.

20 THE COURT: Let me see, does anybody else have any
21 questions? I thought I saw Mr. Snellings --

22 MR. AUSTIN: Well, my comment, that's one of the
23 things -- why Mr. Snellings is rising is pursuant to the
24 agreements that were stated at the telephonic hearing last
25 Friday and today is Mr. Snellings, on behalf of his client, Law

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Austin - Redirect

127

1 Debenture and I believe Ms. Steingart on behalf of Mag Ten, the
2 agreement is that they do not have to participate in the cross
3 examination of the witnesses today. They reserve their right
4 to cross examine the witnesses when we come back for the
5 hearing on October the 6th. And I think they will undertake to
6 let us know whether indeed we need to bring back any or all of
7 these witnesses for that purpose prior to the next hearing.

8 MR. SNELLINGS: That's right. I just want to make
9 sure that was on the record, and we don't want to put it on the
10 record for every witness, but --

11 THE COURT: All right, that's the understanding I have
12 from the hearing we had telephonically last Friday.

13 MR. SNELLINGS: Thank you.

14 THE COURT: That's acceptable.

15 MR. AUSTIN: Thank you, Your Honor.

16 THE COURT: All right, is there anybody else? If not
17 then thank you, Mr. Austin, you may step down. Would this be a
18 good time to take a short break for lunch and then we'll start
19 up again? Who do we have coming next.

20 MR. AUSTIN: We have -- Mr. Hanson will be our next
21 witness, Your Honor, followed by Mr. Byrd and (inaudible).

22 THE COURT: All right, well, we will start again in 1
23 hour. So let's get back in time to do that.

24 ALL: Thank you, Your Honor.

25 (Recess)

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

128

1 THE COURT: Please be seated. All right, are we ready
2 to proceed?

3 MS. DENNISTON: We are, Your Honor.

4 THE COURT: All right, Ms. Denniston?

5 MS. DENNISTON: Thank you, Your Honor. We would call
6 Mike Hanson to the stand at this time.

7 THE COURT: All right Mr. Hanson, come forward to the
8 Courtroom Deputy to be sworn.

9 MIKE HANSON, DEBTOR'S WITNESS, SWORN

10 THE COURT: All right, please speak up clearly, Mr.
11 Hanson, into the microphone.

12 MR. HANSON: Yes, Your Honor.

13 DIRECT EXAMINATION

14 BY MS. DENNISTON:

15 Q. Mr. Hanson, can you state your name for the record please?

16 A. My name is Mike Hanson. Last name is spelled H-A-N-S-O-N.

17 W. And what is your position at Northwestern?

18 A. I'm the Chief Operating Officer.

19 Q. Can you give us a brief description of what your duties and
20 responsibilities are as the Chief Operating Officer?

21 A. As Chief Operating Officer, I'm responsible for the day-to-
22 day operations of the utility business that includes
23 transmission operations, distribution operations, regulatory
24 affairs, government affairs, customer care, as we call it, or
25 customer service, information technology and various support

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

129

1 functions.

2 Q. And how long have you been employed at Northwestern?

3 A. A little over 6 years. I joined the company June 1st in
4 1998.

5 Q. And can you tell us what capacities that you've been
6 employed in at Northwestern?

7 A. Since joining the company I was originally -- my title was
8 President and Chief Executive Officer of the energy division of
9 Northwestern Corporation. And then last year, upon divestiture
10 of the non-utility and consolidation of the corporation to one
11 entity, the utility, I became Chief Operating Officer in
12 August.

13 Q. August of 2004?

14 A. 2000 --

15 Q. 2003.

16 A. 2003, yes.

17 Q. And have you served in that capacity throughout this
18 bankruptcy proceeding?

19 A. Yes I have.

20 Q. And do you expect to continue to serve in that capacity
21 upon the Debtor's exit?

22 A. Yes I do.

23 Q. Can you tell me a little bit about Northwestern's
24 management? I want to talk about the senior management. And
25 basically, can you tell me are you familiar with Northwestern's

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

130

1 senior management?

2 A. Certainly.

3 Q. And you are a part of that senior management team?

4 A. Yes I am.

5 Q. And do you expect the senior management team to continue to
6 manage Northwestern upon exit?

7 A. Yes we do.

8 Q. Can you give the Court a bit of background on each of the
9 individuals that constitute the senior management team?

10 A. Our President and Chief Executive Officer, Gary Drook, has
11 been a Director of the company since 1998. He came on as the
12 President and CEO of Northwestern Corporation January 6th of
13 2003. Gary has over 26 years with regulated utility experience
14 in the telephone industry. He spent a -- that part of his
15 career with the Bell system and eventually what was Ameritech.
16 He retired, I believe it was 1995, from Ameritech and took over
17 an in-bound telemarketing business called Aphena, at which time
18 then he joined the Board and, as I said, came on as President
19 and CEO.

20 I've been in the utility business for almost 24 years;
21 started in the business in the gas construction department of
22 Northern State's Power Company in LaCrosse, Wisconsin back in
23 1981. Went from there to the office doing budgeting and
24 variance analysis while I was completing a degree at UW-
25 Lacrosse. Upon getting my accounting degree from UW-Lacrosse,

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

131

1 I moved to Minneapolis and was in their accounting department
2 and then later became the internal auditor for about 5 years.
3 While I was an internal auditor, I went to law school at
4 William Mitchell College of Law, graduated in May of 1989 and
5 became a regulatory attorney for NSP. Did that for about 5
6 years until January of '94 they appointed me to be the Chief
7 Executive of their South Dakota operations. In 1997 their
8 North and South Dakota operations were combined under me. And
9 then I was recruited by previous management of Northwestern to
10 come in as President and CEO of what was then called
11 Northwestern Public Service in January -- or June, excuse me,
12 of 1998.

13 Brian Byrd is our Chief Financial Officer. He joined our
14 company in December of 2003. He has 18 years of financial
15 management experience with a variety of different companies,
16 from airlines to the Minnesota Vikings, but 7 years of that is
17 in the energy business. He was with NRG, a subsidiary of Excel
18 Energy, and most recently Insight Energy. He joined the
19 company in December.

20 And Roger Schrum, who is our Vice President of Human
21 Resources and Communications has about 20 years of regulated
22 utility experience with Northwestern and Scana in South
23 Carolina.

24 Q. And this would be Northwestern's proposed senior management
25 upon exit?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

132

1 A. That's correct.

2 Q. And was this senior management team involved in the Chapter
3 11 bankruptcy proceeding?

4 A. Yes.

5 Q. With regard to the people that you supervise as the Chief
6 Operating Officer, can you give us a brief overview of your
7 direct reports?

8 A. Yes. Very briefly, starting in the lower left corner, Pat
9 Corcoran is the Vice President of Regulatory Affairs for our
10 entire enterprise, all three states. He has 26 years, all of
11 it in the regulatory department in Montana. Dave Gates is Vice
12 President of Transmission Operations. He also has 26 years of
13 utility experience with Montana Power Company and ourselves.
14 Dave has managed energy supply distribution operations and now
15 transmission operations. Dennis Lopatch, who's called Vice
16 President of Administration, is in charge of government
17 affairs, our lobbying effort, and legal responsibilities in
18 Montana. He was once an attorney for the Montana Public
19 Service Commission and then went and spent the majority of his
20 career with Mountain Bell, later U.S. West, and joined us in
21 2001. Kurt Pole is Vice President of Distribution Operations,
22 Again, for all three states. He resides in Montana. He has 18
23 years of experience, all of it with Northwestern. Bobby
24 Shrapel is Vice President of Customer Care. She has 11 years
25 of utility experience with Minkota Electric Co-Op in Minnesota

Writer's Cramp, Inc.

Certified Court Transcribers

132-329-0191

Hanson - Direct

133

1 and now Northwestern. Bart Thielbar, Vice President of
2 Information Technology has about 18 years of IT experience, 6
3 of that with Northwestern. And Greg Trandon, who's Vice
4 President of Support Services, which is Fleet facilities,
5 supply chain, things of that nature, has 28 years of utility
6 experience with Excel Energy and Northwestern.

7 Q. Okay if we look at this, what's been marked as Debtor's
8 Exhibit-128, can you tell us which individuals have been
9 directly involved in working with Northwestern throughout this
10 bankruptcy proceeding? I think there's a few others.

11 (Debtor's Exhibit-128 previously marked for
12 identification)

13 A. Okay, in terms of the senior management, Gary Drook has
14 been there throughout. I mentioned Brian Byrd joining us in
15 December. I've been there throughout the process, as has Roger
16 Schrum, Eric Jacobson, our general counsel. And Bill Austin,
17 our Chief Restructuring Officer, joined us in April of that
18 year. All of these people have been in their current
19 capacities since before the bankruptcy proceeding began.

20 Q. Okay, and just to sum up with regard to your role as to any
21 of the other senior management, who is the person that's
22 primarily responsible for the -- maintaining the relationship
23 with the regulatory entity?

24 A. That would be myself and Pat Corcoran.

25 Q. Let's talk a little bit about Northwestern's operations.

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

134

1 Can you give us a quick summary of the -- Northwestern Energy's
2 operations?

3 A. We deliver energy, gas and electric energy, to about
4 608,000 customers in three states: Montana, South Dakota and
5 Nebraska. I have the customers broken down in the slide, but
6 we have about 305,000 electric customers in Montana. We have
7 about 7,000 miles of transmission lines in that state. We have
8 58,000 electric customers in South Dakota, and over 3,100 miles
9 of electric transmission lines in that state. Natural gas, we
10 deliver to 163,000 customers in Montana, with 3,500 miles of
11 distribution lines, 2,000 miles of transmission pipeline, and
12 82,000 customers in South Dakota and Nebraska, split roughly
13 equally; there's about 41,000 in each state, 2,100 miles. In
14 each of those we are the transmission and distribution
15 provider. We do not own any production in Montana. We have a
16 small amount of electric production in South Dakota.

17 Q. And how would you characterize Northwestern's business?

18 A. We are a transmission and distribution utility.

19 Q. And what percentage of Northwestern's business is
20 regulated?

21 A. We get over 90% -- I believe it's about 95% of our gross
22 margin comes from the regulated operations.

23 Q. Let's talk just a bit about the energy supply structure.
24 What can you tell us about Northwestern's energy supply
25 structure?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

135

1 A. Well, I'll start first with electric supply because it's a
2 little different in South Dakota than Montana, the two states
3 we have electricity. In South Dakota we do only electric
4 generators, and so we'll describe ourselves as being vertically
5 integrated for electric supply. We don't own fuel sources,
6 coal mines or gas wells, like some utilities. But we own some
7 shares of base load plants of other PE plants, the transmission
8 and distribution lines, and we supply through what are called
9 bundle rates; it's a combined rate for generation and the
10 delivery transmission distribution.

11 In Montana, we are the electric default supplier, as it's
12 called, which means that we procure electricity and deliver it
13 to customers that have not chosen to procure electricity from
14 another source. They may choose to do that, they don't have
15 to. Some states call that the provider of last resort, but we
16 don't own any electric production and we make no margin on that
17 service. We sell the electricity exactly at cost. We do own
18 the transmission and distribution lines and make our margins on
19 the delivery.

20 In natural gas we are the local distribution company in
21 all three states. In Montana, we also serve the role of
22 default supplier, again, for people who have not chosen to buy
23 the commodity from someone else. And in South Dakota/Nebraska,
24 we procure commodity on behalf of customers, deliver it through
25 our pipes to their homes and businesses, and we do earn a small

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

136

1 margin on that in those two states.

2 Q. And how does being a default supply impact Northwestern's
3 business plan?

4 A. Well, it impacts it because we procure -- depending on what
5 commodity prices do over the year, if it's something north of
6 \$400 million a year of natural gas and electricity that we make
7 no margin and it puts risk on us over whether we're going to
8 recover those costs or not.

9 Q. Okay, and what portion of those costs is not recovered?

10 A. We've -- what portion is not recovered? The on the
11 electric side we have not had any disallowances of costs. We
12 do not recover all of our administrative expenses at this time.
13 The cost, for example, of the people doing the procurement
14 activity are not included in the commodity charge; it's a
15 glitch we hope to fix in future rates. In natural gas we have
16 had a recent disallowance of about \$6 million a year for a 2
17 year period, or 12 million, on natural gas. So it's not been
18 large but still \$12 million is a significant amount to us.

19 Q. And how did that become disallowed? Can you give us just a
20 bit of background there?

21 A. Certainly. The Commission, in reviewing our annual gas
22 cost (indiscern.), looked at the way we procured natural gas,
23 determined that we had not replaced what was a fixed price
24 contract with another fixed price contract. That fixed price
25 contract that expired was a buy-back agreement when Montana

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

137

1 Power sold the gas production. And we couldn't replace it in
2 the market anyway, but they determined us to be imprudent in
3 failing to replace that at a fixed price and then imputed a
4 price against us and disallowed the difference.

5 Q. And what has been Northwestern's response, if any?

6 A. Well, our response was to ask for reconsideration, which
7 failed. And we have now appealed that decision to the District
8 Court in the state of Montana.

9 Q. Would it be fair to characterize that as an ongoing
10 dispute?

11 A. It is still continuing, yes.

12 Q. Let's talk briefly about Northwestern's service profile.
13 What can you tell us -- and let's start with Montana -- what
14 can you tell us about Northwestern's service profile in
15 Montana?

16 A. Well, this map depicts the service area we have in Montana;
17 it's about 107,000 square miles. It's the western $\frac{2}{3}$ of the
18 state. The population in that area as of the 2000 census was
19 about 786,000 people, (indiscern.) 305,000 electric customers
20 and 160,000 gas customers.

21 THE COURT: Can we -- excuse me. Can we just take a
22 very short break here? I have another matter I have to take up
23 that'll be very short, I'm so informed.

24 MS. DENNISTON: Thank you, Your Honor.

25 THE COURT: Sorry. Don't leave, Mr. Hanson.

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

138

1 MR. HANSON: Yes Sir.

2 (Recess)

3 THE COURT: Okay, Ms. Denniston.

4 MS. DENNISTON: Thank you, Your Honor.

5 BY MS. DENNISTON:

6 Q. With regard to Montana, can you just -- just to back up and
7 be sure that we're clear. The total population in Montana
8 was what?

9 A. The total population of Montana as of the 2000 census was
10 about 902,000. The areas that we serve at a population of
11 about 786,000. And if you think back to the many miles of line
12 that I talked about, we have a widely dispersed area, a very
13 low customer and low density in Montana. Similarly in eastern
14 South Dakota, we serve roughly the eastern third. The
15 population of the state of South Dakota was 754,000. We serve
16 an area that covers less than 100,000 people; it's about
17 97½ thousand as of the 2000 census. It's a little hard to see
18 on this map, but it'll appear. The reason is we do not serve
19 Sioux Falls, which is right here, the largest city in the
20 state, or the second largest city, Rapid City, out here. But
21 again, many miles of line, low customer density, both states,
22 both gas and electricity in those two areas. And then we serve
23 four communities in central Nebraska: Grand Island, Kearney,
24 North Platt and Aldo, with a combined population of less than
25 100,000, it's about 75,000 people. Just natural gas

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

139

1 distribution in Nebraska.

2 Q. Turning to specifics of electric transmission. What can
3 you tell us about the service territory and electric
4 transmission for Northwestern?

5 A. Well, as this slide points out, 125,000 square miles
6 service area is very large. The two pieces of Montana and
7 South Dakota are in two different reliability counsels. A
8 liability counsel -- Western Electricity Coordinating Counsel
9 in Mid-Common Area Power Pool are power pools where the
10 generation and transmission is all interconnected to maintain
11 stability and reliability of the system. And so they are
12 coordinating operations between all utilities in that region.
13 The two happen to fall into two different reliability counsels.
14 Despite that fact, our System Operation and Control Center in
15 Butte is -- does the system operation and dispatch for our gas
16 and electric operations in all three states. I mentioned
17 earlier that we are not vertically integrated in Montana. We
18 do not have any generation in Montana, we just have
19 transmission and distribution. We do have a small amount of
20 generation in South Dakota. Our System Control Center in
21 Montana also functions as what's called a control area
22 operator. And what a control area operator does is the one who
23 actually dispatches the power plants to match the generation to
24 the load at every moment of every day. So notwithstanding that
25 we don't own it, we are directing the owners of the plant of

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

140

1 what load to carry and what power plants to run. We have
2 almost 7,000 circuit miles in Montana and 1,300 in South
3 Dakota.

4 Q. Let's talk just a bit about the gas transmission and
5 storage. What can you tell us about Northwestern's gas
6 transmission and storage?

7 A. Well, we have a very extensive transmission -- gas
8 transmission system in Montana, with about 2,000 miles of gas
9 transmission pipe. There are six interconnections, four of
10 them that are significant: TransCanada Pipeline coming out of
11 Alberta to the north, Colorado Interstate Gas coming up from
12 Wyoming to the south, the Williston Base and Interstate
13 Pipeline -- well, pick up the pace, I take it.

14 (Laughter)

15 Q. Sorry about that, Mike.

16 THE COURT: Ah, technology.

17 MS. DENNISTON: I hear Mr. Austin sitting over there
18 thinking, "I told you so."

19 (Court and counsel confer)

20 MS. DENNISTON: There you go, Mike.

21 A. I was describing the significant pipeline interconnections.
22 Williston Basin Pipeline to the northeast, and Cana Gathering
23 System also in Canada. Energy West and Haver Pipeline are
24 small interconnections within the state of Montana. We also
25 happen to have about 17 BCF of storage. To put that into

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

141

1 perspective, the annual gas load for our customers in Montana
2 is about 22 BCF. So you can store not quite a year's worth of
3 gas. What this allows us to do is deliver from the Rockies
4 Production Zone or the Canadian Production Zone into the state.
5 In just rough terms to put it into perspective, the gas
6 transmission and distribution constitutes about 25% of our
7 gross margin. Electric distribution and transmission is about
8 75%.

9 Q. Let's talk a bit about the South Dakota generation. You
10 mentioned briefly that there was some generation in South
11 Dakota. What can you tell us about that?

12 A. We own -- we are a minority interest holder of three base
13 load coal generating units: One of them Cayota Station up in
14 North Dakota, the Big Stone Plant in eastern South Dakota, and
15 a portion of Neo Unit in Iowa. Cayota and Big Stone are
16 operated by Outerdale Power Company, the Neo Unit by Mid-
17 American. So we're a non-operating minority holder. We don't
18 operate the plants. In total, 208 megawatts of base load
19 generation. We also have about 119 megawatts of small gas and
20 oil fired peaking units that are throughout our territory, so
21 we own a total of, you know, just under 327 megawatts, but
22 we're not an operator of power plants, per se. The electric
23 generation that we own constitutes less than 5% of our revenue
24 and margin on the company as a whole.

25 Q. And do you have an understanding of how this ownership

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

142

1 impacts Northwestern's valuation?

2 A. I'm not an expert on valuation, but since it's such a small
3 part, less than 5%, I wouldn't think it'd have any material
4 effect on the valuation.

5 MS. DENNISTON: And for the record, Your Honor, we're
6 skipping slide #40 as we've already covered the electric system
7 and distribution system, just so that the record's clear.

8 BY MS. DENNISTON:

9 Q. Mr. Hanson, are you familiar with the other utility
10 companies in the industry that have both gas and electric
11 distribution?

12 A. Most of them.

13 Q. And do you have an understanding as to whether or not they
14 have a similar ratio of -- if I were to ask you, similar ratio
15 of gas to electric?

16 A. For many of them --

17 Q. For example --

18 A. -- some do, some don't.

19 Q. -- Vectron.

20 A. Yes.

21 Q. How is Vectron compared to Northwestern?

22 A. Vectron is almost the opposite. They're in Indiana and
23 Ohio and they get about 70% of their revenue from gas and 30%
24 from electric. We're almost the inverse. We get about 75 from
25 electric and 25 from gas.

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

143

1 Q. Okay. And I believe you testified earlier that
2 Northwestern was how much -- what percentage regulated?

3 A. It's about 95%.

4 Q. And do you have an understanding as to the other -- some
5 of the other utility companies in the industry as to their
6 percentage of regulation versus non-regulated activity?

7 A. I have reviewed many of them and I do, yes.

8 Q. And what do you -- if I were to ask you what would be the
9 difference on Allegheny Energy?

10 A. Well, Allegheny as an example, in 2003 got about 40% of
11 it's revenues from non-regulated operations.

12 Q. And how about Synergy Corporation?

13 A. Synergy about -- not quite 40, 37% I believe.

14 Q. And how about PNM Resources?

15 A. PNM also had about 37% from non-regulated activities.

16 Q. And in your roll as the Chief Operating Officer, do you
17 keep up to date with the various industry periodicals and trade
18 magazines?

19 A. Certainly.

20 Q. And do you review those on a regular basis?

21 A. Yes I do.

22 Q. With regard to -- I want to switch now -- switch gears and
23 talk a little bit more about the specifics of the regulation
24 that Northwestern has to contend with. What can you tell us
25 about the Federal Energy Regulatory Commission?

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

144

1 A. Well, the Federal Energy Regulatory Commission regulates
2 energy transactions in interstate commerce basically. And so
3 if sales of electricity -- what we would call wholesale sales
4 or sales to other utilities are deemed to be an interstate
5 commerce and regulated by the FERC, as is transmission --
6 electric transmission or gas transmission sales to other
7 utilities.

8 Q. And who at Northwestern is the primary person that
9 interacts with FERC?

10 A. Pat Corcoran.

11 Q. And are you -- do you supervise Mr. Corcoran?

12 A. I do, yes.

13 Q. So would you consider yourself to be up to date on
14 activities as between Northwestern and FERC?

15 A. Yes.

16 Q. And can you tell us how you would characterize the
17 relationship Northwestern has with FERC?

18 A. The relationship and regulatory environment with FERC is
19 stable. We don't have any major issues or controversies
20 recently or pending with FERC.

21 Q. Northwestern is also subject to another layer of
22 regulation, is it not?

23 A. Yes, state regulation.

24 Q. What can you tell us about the state regulation?

25 A. Well, each of the state public service or public utility

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

145

1 commissions regulate the rates and terms and conditions of
2 service within their state. They have varying jurisdiction on
3 other matters. For example, Montana has jurisdiction to
4 oversee financing and the capital structure of the company
5 whereas the others do not. But they all regulate the rates
6 that we charge to retail customers and the terms, the tariff
7 conditions, for those services.

8 Q. Okay, and with regard to Montana Public Service Commission,
9 who is the primary person at Northwestern responsible for that
10 relationship?

11 A. That is Pat Corcoran and myself.

12 Q. Okay, and would you say -- are you up to date on the status
13 of the relationship as between Northwestern and the Commission?

14 A. Yes.

15 Q. And how would you describe the relationship Northwestern
16 has with the Commission?

17 A. The environment in Montana has been very challenging I
18 would say. We've had a large number of issues, matters before
19 the Commission. The Commission has had a long history before
20 Northwestern acquired Montana Power of a -- what I would say
21 more consumer-oriented results, meaning less favorable to the
22 company. I might contrast that with South Dakota in
23 particular. We've had a long environment in South Dakota with
24 very little issues and controversy. The Nebraska Public
25 Service Commission is fairly new. It's been around just less

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

146

1 than 2 years, but we've established a pretty good rapport with
2 that Commission and, again, have no major issues or
3 controversies pending in Nebraska.

4 Q. And are you familiar with the stipulation and settlement
5 that the Debtor has entered into as between the Debtor, the
6 Public Service Commission from Montana and the Consumer's
7 Counsel?

8 A. Yes I am.

9 Q. Were you involved in the negotiations leading up to that
10 stipulation?

11 A. Yes I was.

12 Q. What can you tell us about how that stipulation has
13 impacted the relationship between Northwestern and the Montana
14 Public Service Commission?

15 A. Well, the stipulation certainly resolves a number of issues
16 that were raised by the Commission and the Montana Consumer
17 Counsel in this bankruptcy proceeding. It does not resolve all
18 of the issues and controversies that we have pending before
19 that Commission.

20 Q. And what did the Debtor accomplish by entering into that
21 stipulation?

22 A. Well, the main accomplishment in resolving these issues was
23 to get the Commission and Consumer Counsel support, or at least
24 they're no longer objecting to our Plan of Reorganization, and
25 they are and have authorized the financing activities necessary

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

147

1 to effectuate that Plan.

2 Q. And do you know if the Public Service Commission has
3 entered a order approving stipulation?

4 A. Yes, they just recently did that.

5 Q. Let's talk about some of the issues or some of the points
6 under the stipulation. What is the impact of the ring fencing
7 component?

8 A. Well, let me first describe what's meant by the term. Ring
9 fencing is structurally separating ownership of utility assets
10 from non-utility assets. So under this stipulation, the parent
11 company of Northwestern will own only regulated utility assets.
12 Any non-utility or non-regulated assets we may own will be
13 relatively minor, but they will be held in subsidiary
14 companies. Any debt that we take on at the parent company to
15 finance the activities of the utility cannot be used to fund
16 non-utility activities except for a limited investment basket,
17 which I'll describe in just a second. Any debt associated with
18 the non-utility subsidiaries must be non-recourse to the parent
19 and you can't have cross default provisions, things of that
20 nature. This limited investment basket is -- starts out at \$60
21 million, and that was created in order to allow the company to
22 provide basically working capital support for the small non-
23 utility subs that it does have. If any assets are divested,
24 whether they be utility assets of the parent or non-utility at
25 one of the subs, debt attached to that or associated with --

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

148

1 must follow the asset. Another pretty significant provision, I
2 think, is that the Commission will not institute a rate review
3 any sooner than the fall of 2006. We are required by September
4 of that year to file rate information based on a 2005
5 (inaudible) as it's called with the Commission and the Consumer
6 Counsel. It is not clear whether there will be any party
7 seeking a change in rates. If there is a party, ourselves or
8 the Consumer Counsel for example, that party bears the burden
9 of proof. But with that, we know that rates will not be
10 changed any sooner than 2007, following the review period from
11 this filing.

12 Q. So in connection with the time period between now and that
13 filing the rates won't go up or down?

14 A. Our T&D rates will not go up or down. The commodity costs
15 are collected through a past supervision not covered by this
16 (inaudible). T&D rates we earn our margin or profit on will
17 not go up or down in that period.

18 Q. In connection with the stipulation, how would you
19 characterize whether Northwestern's receiving a greater or
20 lesser degree of regulation?

21 A. Well, I think in many respects a greater degree because
22 with this stipulation we have various filing requirements,
23 information; we've got to keep them informed. The Commission
24 apparently takes a view that gives them an active role in
25 anything from management of the company to ownership. There

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

149

1 was a recent public statement covered in the press in Montana
2 that the Commission believes that if the company were to be
3 sold that it has the right to approve the sale and is proposing
4 that it create criteria by which it will judge the fitness of
5 any prospective buyer. Another issue not on the slide, but we
6 were asked in conjunction with the stipulation to do a -- to
7 hire a third party to assess the condition of our plant, our
8 physical plant, the transmission and distribution systems, gas
9 and electric. We retained a firm by the name of Liberty
10 Consulting to do that. And now we need to file a follow-up
11 report with the Commission, and they're going to monitor our
12 progress in implementing any changes to our maintenance or
13 construction activities.

14 Q. Have you had a chance to review the Liberty Consulting
15 Group's report?

16 A. Yes, certainly. In great detail.

17 Q. And have you made a determination as to what the impact is
18 going to be on Northwestern from a cash flow perspective?

19 A. We haven't come up with a final figure. Some of the
20 activities that are recommended are covered within our current
21 budget, they're just a change in approach. Others are going to
22 require additional resources. But I would say that without
23 question it's going to put some upward pressure on our costs,
24 both from an operating expense standpoint and in capital
25 expenditure standpoint. Some of those we may be able to offset

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191

Hanson - Direct

150

1 with other (inaudible). As of right now, we do not have an
2 assessment of the total impact.

3 THE COURT: Excuse me for just a moment. We are
4 getting a good deal of interference on the telephone lines, so
5 it sounds as if there's either a bad connection or maybe
6 somebody is shuffling something. I must advise you that if
7 this continues, I'm going to require that the telephone
8 connection be terminated and re-established. We're hearing it
9 right now. So the next time that happens, we're going to
10 terminate the telephone line --

11 (Telephone interference continues)

12 THE COURT: Let's do it. Let's terminate the
13 telephone connection and set it up again. Everybody on the
14 telephone, you are being terminated at this moment.

15 (Telephone connections terminated)

16 THE COURT: All right, I think we can go ahead and
17 proceed. My view of the world is that anybody who is on the
18 telephone takes the risk of technology, and so let's not waste
19 everybody else's time here. We'll try to get that hooked up
20 again. How as -- who was in charge of doing that, somebody at
21 the Debtors -- who hooked up this?

22 MS. DENNISTON: I think -- Mr. Chipman, do you know
23 anything about this?

24 (Laughter)

25 (Counsel confer)

Writer's Cramp, Inc.

Certified Court Transcribers

732-329-0191